Afternoon Session on the Railroad Rehabilitation and Improvement Financing (RRIF) Program

RRIF Overview

Ms. JoAnne McGowan, Chief of the Freight Programs Division of the Federal Railroad Administration (FRA), provided an overview of RRIF. Ms. McGowan began by noting that the purpose of her presentation was to stimulate discussion and generate ideas from the audience.

Ms. McGowan noted that the Transportation Equity Act for the 21st Century (TEA-21) established RRIF, a Federal credit program administered by the Federal Railroad Administration (FRA).

Ms. McGowan stated that under RRIF the DOT Secretary may provide direct loans and loan guarantees for terms up to 25 years for the acquisition, development, improvement, or rehabilitation of intermodal or rail equipment or facilities, including track, bridges, yards, buildings, and shops. The interest rate on loans will be set at the U.S. Treasury rate for comparable-term securities.

Ms. McGowan noted that eligible recipients included State and local governments, government-sponsored authorities and corporations, and railroads and joint ventures that include at least one railroad. Both public and private entities are eligible for assistance under RRIF.

Ms. McGowan noted that statutory priority has been given to projects which:

- enhance safety;
- enhance the environment;
- promote economic development;
- are included in State transportation plans;
- promote U.S. competitiveness; and
- preserve/enhance service to small communities and rural areas.

The criteria listed above are not prioritized. Conference participants were welcomed to provide input on which priorities should be given the most weight during the project selection process.

Ms. McGowan said that Congress imposed a funding limitation on RRIF. The statutory funding limitation capped the aggregate balance of outstanding debt at $3.5 billion, with $1 billion being reserved for shortline and regional railroads.

Ms. McGowan stated that under RRIF credit risk premiums would be paid up front by project sponsors. The credit risk premium equals the net present value of expected losses due to default, delinquency, prepayment, interest rate subsidy, and other factors. Credit risk premiums cannot be captured through interest rate adjustments.

Ms. McGowan noted that implementing regulations are currently being developed for RRIF, and must be approved by the Administration before being issued. No loan commitments can be made prior to the issuance of regulations. The unique feature of the credit risk premium being paid by a non-Federal source may add time to the approval of regulations.

Ms. McGowan stated that on July 16th FRA published a Federal Register notice on RRIF. The notice requested expressions of interest from potential applicants. To date, FRA has received input from 11 State Departments of Transportation, 17 small railroads, and seven local governments.

Ms. McGowan noted that based on the data received, total needs may exceed $3 billion. There is clearly insufficient capacity to fund railroad improvements using traditional grants.

Discussion

A member of the audience asked if safety projects will be eligible for assistance under RRIF.

Ms. McGowan responded that safety projects will be given a high priority for funding under RRIF.

An audience member asked if highway/railroad grade separation projects would be eligible for assistance under RRIF.

Ms. McGowan responded that grade separation projects were eligible. These projects are also eligible for assistance under TIFIA.

A member of the audience commented that TEA-21 established a $3.5 billion ceiling on aggregate outstanding debt under RRIF. Does the $3.5 billion represent a cap on outstanding debt at any given point in time, or is it a one time infusion?

Ms. McGowan responded that the $3.5 billion represents a maximum aggregate unpaid balance. As direct and guaranteed loans are repaid, room will be made under that cap for more debt.

An audience member stated that FRA could make RRIF more attractive if it returned unused credit risk premiums to projects that meet their financial obligations.

Ms. McGowan stated that in order to minimize risk to the Federal Government, loans and loan guarantees will be placed in cohorts. When all obligations attached to the cohorts have been satisfied, funds that are not used to cover default costs may be returned to project sponsors on a pro rata basis.

A member of the audience asked for a clarification on the loan guarantee provisions under RRIF.

Ms. McGowan said that loan guarantees from the Federal Government to private lenders will attract private capital on similar terms as direct loans. The interest rate on the private loan will be negotiated between project sponsor and lender, but must be approved by DOT.

An audience member asked for clarification on the Federal Government's position in the event of default.

Ms. McGowan noted that the RRIF statute requires FRA to establish default regulations. Once established, the default regulations will guide FRA through the process. However, based on FRA's interpretation of the Office of Management and Budget's (OMB) Circular A-129, the Federal Government must have a priority claim on project assets in the event of default.

An audience member asked for clarification on how the Federal Government would cover default losses.

Ms. McGowan stated that loans will be placed in cohorts, or groups. The credit risk premiums paid up front by the project sponsors will be pooled to cover the expected losses resulting from defaults within each cohort. Once all the financial obligations have been met for the loans in the cohort, the funds not used to cover default losses may be returned to the original source (projects that do not default) on a pro rata basis.

A member of the audience asked if a public agency would be allowed to pay the credit risk premium for a private entity if the project benefited the public.

Ms. McGowan stated that FRA encourages private and public sector cooperation and sharing of financial resources.

An audience member asked if there would be any way to fund the credit risk premium which did not involve an up front cash payment.

Ms. McGowan responded that FRA would only accept up front cash payments.

A member of the audience stated that the Treasury rate is lower than comparable-term private securities. This fact will drive project sponsors to obtain as much assistance from FRA as possible, while minimizing their private debt.

Ms. McGowan responded that although the Treasury rate is lower, the private banks will not charge a credit risk premium that must be paid up front. In other words, there are tradeoffs.

A member of the audience asked if projects would bear any liability in the event of default.

Ms. McGowan stated that liability and collateral would be established in the loan agreement signed by both the project sponsor and the Federal Government.

An audience member stated that the risk premium rebate provision covered previously in the discussion could result in net losses for the Federal Government. The rebate provision means that every successful cohort will trigger a rebate to project sponsors while losses resulting from defaults in unsuccessful cohorts will be absorbed by the Federal Government.

Ms. McGowan responded that although the authorizing legislation does provide for the possibility of rebates, in practice they are unlikely to occur. FRA has engaged Ernst & Young as a financial consultant to assist in developing economic models which will enable FRA to appropriately estimate default losses.

A member of the audience stated that if rebates are unlikely to occur, FRA may want to consider abandoning the concept before it provides draft implementing regulations to OMB. OMB would most likely not approve of the rebate, and may establish prohibitively expensive credit risk premiums to cover expected losses.

Ms. McGowan responded that FRA could not ignore the rebate concept because it was established in statute.

Ms. Kim Burke, Ernst & Young, stated that each cohort will undergo annual default re-estimation. As default risk diminishes over time, credit risk premiums will not revert to the Treasury but will instead be set aside in accounts established for each cohort. The cohort and rebate concepts are in compliance with the Federal Credit Reform Act of 1990 and OMB Circular A-129.

An audience member asked if projects receiving assistance under RRIF would be allowed to partner with foreign firms and governmental agencies.

Ms. McGowan stated that there is nothing in the RRIF statute that would prohibit projects from participating in international partnerships.

Ms. McGowan closed the discussion by thanking the focus group participants for their valuable input, and commenting that they were welcome to provide more input in the coming months.